

Decision PROPOSED DECISION OF ALJ SIMON (Mailed 8/21/2007)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to
Implement the California Renewables
Portfolio Standard Program.

Rulemaking 04-04-026
(Filed April 22, 2004)

OPINION ON PETITION FOR MODIFICATION OF DECISION 05-12-042

Summary

We grant the request of the California Wind Energy Association (CalWEA) and the Green Power Institute (GPI) that the 2007 market price referent (MPR) developed for the renewables portfolio standard (RPS) program include an additional element in the MPR to account for the costs of the emission of greenhouse gases (GHG adder). Although we deny at this time their request to modify the MPR methodology set forth in Decision (D.) 05-12-042 to include a GHG adder for 2008 and later years using the specific approach adopted here, we intend to examine the MPR for 2008 and later years to determine what changes should be made to the MPR methodology, including how the costs of GHG emissions should be reflected in the MPR for 2008 and later years.

Procedural Background

We set the initial parameters for the MPR in D.03-06-071. We first developed the method for calculating the MPR in D.04-06-015. In D.05-12-042, we expanded and stabilized the methodology for calculating the MPR. This

methodology has been used for the 2005 MPR (Resolution E-3980 (April 13, 2006)) and the 2006 MPR (Resolution E-4049 (December 14, 2006)).

On June 25, 2007, CalWEA and GPI (collectively, CalWEA) filed the Petition of the California Wind Energy Association and the Green Power Institute for Modification of Decision 05-12-042: Interim Opinion Adopting Methodology for the 2005 Market Price Referent (Petition). The Petition requests that we modify D.05-12-042 to include a GHG adder in the MPR for 2007 and all subsequent years.¹

Responses were timely filed on July 17, 2007 by the California Cogeneration Council (CCC), Center for Energy Efficiency and Renewable Technologies (CEERT), Concentrated Solar Power Alliance (CSPA), Division of Ratepayer Advocates (DRA), Pacific Gas and Electric Company (PG&E), San Diego Gas & Electric Company (SDG&E), Southern California Edison Company (SCE), and Union of Concerned Scientists (UCS). CalWEA timely filed its reply on July 24, 2007.

¹ The Petition was accompanied by a Motion of the California Wind Energy Association and the Green Power Institute for Expedited Decision and Order Shortening Time Related to its Concurrently Filed Petition for Modification of Decision 05-12-042: Interim Opinion Adopting Methodology for the 2005 Market Price Referent. The Administrative Law Judge's Ruling on the Motion to Expedite (June 28, 2007) provided that the time for responses and reply be shortened. Responses were to be filed and served not later than July 17, 2007, and the reply of CalWEA and GPI was to be filed and served not later than July 24, 2007.

Discussion**1. Timeliness of Petition**

A petition for modification must ordinarily be filed within one year of the decision for which modification is sought. "If more than one year has elapsed, the petition must. . . explain why the petition could not have been presented within one year of the effective date of the decision." Rule 16.4(d), Rules of Practice and Procedure.² Since CalWEA's Petition was filed more than 18 months after the effective date of D.05-12-042, CalWEA is obligated to explain the lapse of time.

In D.05-12-042, we concluded that the request of UCS, DRA, and GPI to have a GHG adder as a component of the MPR was premature. We indicated our willingness to consider a GHG adder at a later time, once the then-current GHG policy discussions were "translated into regulatory programs or other sufficiently concrete market impacts. . ." (D.05-12-042, *mimeo.*, p. 48.)

CalWEA asserts that this condition was not met until January 1, 2007, the effective date of California's landmark GHG regulation initiatives: Assembly Bill (AB) 32 (Nuñez/Pavley), 2006 Stats. ch. 488, and Senate Bill (SB) 1368 (Perata), 2006 Stats. ch. 598. No other party disputes CalWEA's choice of this date as the earliest time it would have been reasonable to seek modification of D.05-12-042 to include a GHG adder. Since even this earliest possible date is more than one

² Unless otherwise indicated, all subsequent citations to rules refer to the Rules of Practice and Procedure, which are codified at Chapter 1, Division 1 of Title 20 of the California Code of Regulations, and citations to sections refer to the Public Utilities Code.

year after the effective date of D.05-12-042, CalWEA has complied with the requirements of Rule 16.4 to justify the late submission of its Petition.

2. The MPR

We reviewed the history of the MPR in D.05-12-042. The MPR is the result of the Legislature's direction, in § 399.15(c), that we “establish a methodology to determine the market price of electricity. . .” for use in the RPS program.³ The MPR applies to long-term RPS procurement contracts (*i.e.*, contracts of at least 10 years in duration) between investor-owned utilities and RPS-eligible generators. In calculating the MPR for each RPS procurement year, Energy Division staff provides values for procurement contracts of 10, 15, and 20 years' duration.

We initially determined, in D.03-06-071, that the market in long-term fixed-price contracts for electricity was dominated by the contracts previously

³ In full, § 399.15(c) provides that this Commission, in consultation with the California Energy Commission (CEC), must:

Establish a methodology to determine the market price of electricity for terms corresponding to the length of contracts with renewable generators, in consideration of the following:

- (1) The long-term market price of electricity for fixed price contracts, determined pursuant to the electrical corporation's general procurement activities as authorized by the Commission.
- (2) The long-term ownership, operating, and fixed-price fuel costs associated with fixed-price electricity from new generating facilities.
- (3) The value of different products, including baseload, peaking, and as-available output.

signed by the Department of Water Resources (DWR), and that the utilities did not have a sufficient number of existing long-term contracts outside the DWR process for us to use as the basis for the MPR. We therefore chose to base the MPR on the "costs associated with fixed-price electricity from new generating facilities." (§ 399.15(c)(2).) In D.04-06-015, we developed a model of a new combined-cycle gas turbine (CCGT) generating facility to serve as a "proxy plant" with which to model the costs that would be part of the MPR. We refined and extended the model in D.05-12-042.

3. California's GHG Policy Mandates

CalWEA asserts that AB 32 and SB 1368, taken together, "commit California to a comprehensive regulatory program to reduce GHGs." (Petition, p. 3.) AB 32 requires the Air Resources Board (CARB) to develop comprehensive regulation of GHG emissions, to be operative not later than January 1, 2012. (Health & Safety Code § 38562.) CARB is required to consult with this Commission and the CEC in developing its GHG regulations. In Rulemaking (R.) 06-04-009, we are developing our recommendations to CARB. In D.07-01-039, we implemented interim GHG emissions performance standards for long-term financial commitments to baseload generation by California load-serving entities (LSEs), as required by SB 1368.

CalWEA further notes that we have for some time recognized the importance of accounting for GHG emissions by using a GHG adder as an evaluative tool in a variety of contexts. These include the long-term procurement activities of utilities (D.04-12-048); the energy efficiency programs of utilities (D.05-04-024); and the cost-effectiveness of nuclear power plant refurbishment by utilities (D.05-12-040).

CCC, CEERT, CSPA, DRA, and UCS support CalWEA's view that the legislative mandates embodied in AB 32 and SB 1368 have created a regulatory environment in which the costs of GHG emissions should be recognized in the MPR.

PG&E, SDG&E, and SCE all disagree with this view. They argue that because the policy requirements of the recent GHG emissions reduction legislation have not yet been fully translated into regulatory requirements, we should refrain from including a GHG adder in the MPR at this time. They note that in D.05-12-042, we declined to use the evaluative GHG adders adopted in D.04-12-048 and D.05-04-024 as the basis for a GHG adder in the MPR. They urge that it continues to be premature to include a GHG adder in the MPR.

The utilities' arguments fail to take into account the new reality of GHG emissions regulation in California. The mandates of AB 32 and SB 1368 make the present moment – and the future – different from the situation in December 2005. At the time we issued D.05-12-042, no requirements had yet emerged from the aspirations for a comprehensive GHG emissions policy in California and the many efforts to develop one. Just over a year later, we issued D.07-01-039, implementing SB 1368.⁴ We are also actively working with CARB and the CEC to meet the Legislature's deadline of January 1, 2012 for California's enforceable limits on GHG emissions.

⁴ SCE correctly notes that the interim emissions performance standard articulated in D.07-01-039 does not impose current costs on a new CCGT, but fails to acknowledge that D.07-01-039 is only the first, not the last, California regulatory response to GHG emissions from fossil-fueled generation.

The MPR applies to long-term contracts for RPS-eligible generation. As UCS points out, even the shortest of these contracts will continue for years after California's binding GHG rules are in effect. For example, more than two-thirds of the duration of a 10-year contract signed in 2007 and beginning deliveries in 2009 will occur after January 1, 2012. For longer contracts, the proportion of the contract in the period after January 1, 2012 is even larger. The CCGT proxy plant used in the MPR calculations will have similarly long post-2012 contract durations.⁵

The utilities overstate the significance of GHG control costs being imposed in the future. The most significant parameter in the MPR, natural gas prices, is a projection of costs to be incurred in the future, beginning with the on-line date of the project, which often is several years into the future. The GHG adder is similarly a projection of costs to be incurred in the future, beginning with the conservatively estimated "on-line date" of GHG control costs in California.

Nor is it relevant, as SCE insists, that the decision about the electricity sector point of regulation for GHG emissions (whether load-based or generator-based) will not be made prior to adoption of the 2007 MPR. SCE has provided no reason to believe that a regime with a load-based cap would not create GHG compliance costs (whether through technological controls or purchases of allowances) for natural gas-fueled generation, in order to bring the generator's

⁵ The MPR must use contract terms "corresponding to the length of contracts with renewable generators. . ." § 399.15(c).

carbon profile into the range that would be reasonable for a retail seller to add to its portfolio.⁶

In addition, for MPR purposes, it is not particularly relevant which party bears the cost of GHG compliance in the system, since ratepayers will eventually pay for increased GHG compliance costs. The MPR is used to determine the costs of RPS contracts that will be recovered by the utilities through rates. Since GHG compliance costs are reasonably foreseeable in light of AB 32 and will be passed through to ratepayers regardless of the point of regulation, our present uncertainty about the point of regulation should not prevent taking account of these costs through a GHG adder in the 2007 MPR.

We cannot ignore the long-term nature of the MPR simply because we are in the early stages of California's development of binding GHG emissions limits. As CalWEA points out, the potential complexities of the details of that regulatory development could provide an excuse to avoid addressing GHG costs in the MPR for many years. We believe that we can and should adopt a stance more in keeping with the reality of GHG regulation in California, while still taking a measured approach to the further development of the MPR.

We will therefore adopt a GHG adder for the 2007 MPR, but we will not at this time modify D.05-12-042 to make a more permanent change to the MPR methodology to include a GHG adder as proposed by CalWEA. We intend, instead, to examine the MPR for 2008 and later years to determine what changes

⁶ We note that, in R.06-04-009, SCE urges us to adopt an approach in which generators would be the point of GHG regulation and would bear the direct "out of pocket" expenses. See Reply of Southern California Edison Company to Comments and Legal Briefs on Market Advisory Committee Report (Aug. 15, 2007).

should be made to the MPR methodology, including how the costs of GHG emissions should be reflected in the MPR for 2008 and later years.

4. Timing of GHG Costs

CalWEA proposes two options for calculating the GHG adder: (1) the CCGT proxy plant incurs GHG emissions costs beginning in 2007, or, the more conservative option, (2) the CCGT proxy plant incurs GHG emissions costs beginning in 2012.⁷ DRA supports choosing the first option, that costs are first incurred by the proxy CCGT plant in 2007. UCS suggests the use of a "conservative" GHG adder value, but does not identify which initial year of incurred costs it would choose. No other party responds to this issue.

We believe that the later date is more realistic in light of current regulatory requirements. New CCGTs are not affected by the interim emissions performance standard set forth in D.07-01-039, but gas-fired generation will eventually be part of overall regulation of GHG emissions in the production of electricity. We therefore adopt, for the 2007 MPR only, a GHG adder reflecting GHG control costs for a CCGT proxy plant beginning January 1, 2012.⁸

5. Value of GHG Adder

CalWEA proposes using a GHG adder based on the model developed by Energy and Environmental Economics (E3) and adopted in D.04-12-048 and D.05-04-024. DRA and UCS support using these values; CEERT accepts their use on an interim basis.

⁷ These options are presented, with sample dollar amounts, in Table 1 and Table 2, respectively, at p. 10 of the Petition.

⁸ CalWEA properly recognizes that the MPR methodology requires that these costs must be levelized throughout the term of the contract.

As UCS points out, the E3 model has been used in a variety of Commission proceedings and has been subject to extensive review by parties in those proceedings. Since no party responding to the Petition has objected to the use of the E3 model for values for GHG emissions costs for the 2007 MPR, we will adopt the E3 model for calculating the GHG adder for the 2007 MPR.

6. Next Steps

CalWEA asks that we modify D.05-12-042 to make the use of the E3 model adopted in D.04-12-048 a permanent feature of the MPR methodology. UCS endorses the E3 model but urges us to revisit the GHG adder as more information becomes available. CSPA and CEERT ask us to undertake a comprehensive review of the MPR in 2008. PG&E believes that the 2008 MPR would be a more appropriate vehicle for addressing GHG issues than the 2007 MPR.

The E3 model provides a sound basis for a GHG adder for the 2007 MPR. We also agree with those parties suggesting that we take a more deliberate approach to making a more permanent change to the MPR methodology to account for GHG emissions. We will therefore authorize the use of the E3 model for calculating a GHG adder for the 2007 MPR only. We also authorize the assigned Commissioner and assigned administrative law judges in R.06-02-012, in R.06-05-027, and/or their successor proceedings, to set a schedule for examining the MPR for 2008 and later years for purposes of determining what changes should be made to the MPR methodology, including how the costs of GHG emissions should be reflected in the MPR for 2008 and later years.

Comments on Proposed Decision

The proposed decision of the Administrative Law Judge in this matter was mailed to the parties in accordance with Section 311 of the Public Utilities Code

and comments were allowed under Rule 14.3 of the Commission's Rules of Practice and Procedure. Comments were filed on September 10, 2007 by CalWEA, GPI, and CSPA jointly (CalWEA) and by SCE. Reply comments were filed on September 14, 2007 by DRA.

CalWEA supports the PD but expresses concern that the calculation of the 2007 MPR may not be coordinated with our order on the petition for modification. We believe that Ordering Paragraph 1, below, provides adequate assurance on this point.

SCE reiterates its position that it is premature to include a GHG adder in the 2007 MPR, both because GHG control costs are not sufficiently definite and because the point of GHG regulation has not yet been decided. DRA, in reply, asserts that under any GHG regulatory regime, a generator emitting GHGs will ultimately incur costs to continue to emit at the same level; those costs will be passed on to the users of the electricity. We agree with DRA, and will employ a GHG adder in the 2007 MPR. We have expanded the discussion in the text to make our reasoning more accessible.

Assignment of Proceeding

Michael R. Peevey is the assigned Commissioner and Anne E. Simon is the assigned Administrative Law Judge in this proceeding.

Findings of Fact

1. AB 32 provides that GHG emissions limits shall be adopted by CARB and shall become operative by January 1, 2012.
2. In D.07-01-039, the Commission established interim GHG emissions performance standards for long-term financial commitments of California LSEs for baseload generation, as required by SB 1368.

3. Any RPS procurement contract subject to the 2007 MPR will continue for many years past January 1, 2012.

4. The E3 model for calculating GHG emissions costs has been reviewed and accepted in several Commission proceedings.

5. It is reasonable to include in the 2007 MPR a calculation of GHG emissions costs to be incurred by the MPR proxy CCGT beginning January 1, 2012.

6. It is reasonable to review the role of a GHG adder in the MPR for 2008 and later years separately from a determination of whether to include a GHG adder for the 2007 MPR only.

Conclusions of Law

1. The 2007 MPR calculation should use the E3 model for calculating GHG emissions costs to be incurred by the MPR proxy CCGT beginning January 1, 2012.

2. The assigned Commissioner and assigned administrative law judges in R.06-02-012, in R.06-05-027, and/or their successor proceedings, should be authorized to set a schedule for examining the MPR for 2008 and later years for purposes of determining what changes should be made to the MPR methodology, including how the costs of GHG emissions should be reflected in the MPR for 2008 and later years.

3. In order to allow the 2007 MPR to be calculated expeditiously and negotiation of RPS procurement contracts from the 2007 solicitation to proceed expeditiously, this order should be effective immediately.

O R D E R

IT IS ORDERED that:

1. The calculation of the 2007 market price referent (MPR) used in the renewables portfolio standard program shall use the model for calculating greenhouse gas emissions costs (GHG adder) developed by Energy and Environmental Economics and adopted in Decision 04-12-048, applied to the MPR's combined cycle combustion turbine proxy plant for GHG emissions costs beginning January 1, 2012.

2. The assigned Commissioner and assigned administrative law judges in Rulemaking (R.) 06-02-012, in R.06-05-027, and/or their successor proceedings, may set a schedule for examining the MPR for 2008 and later years for purposes of determining what changes should be made to the MPR methodology, including how the costs of GHG emissions should be reflected in the MPR for 2008 and later years.

3. In all respects other than those set forth in Paragraphs 1 and 2, above, the Petition of the California Wind Energy Association and the Green Power Institute for Modification of Decision 05-12-042: Interim Opinion Adopting Methodology for the 2005 Market Price Referent is denied.

This order is effective today.

Dated _____, at San Francisco, California.